

Internal Revenue Service

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Department of the Treasury
Washington, DC 20224

Third Party Communication: None
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Person To Contact:
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Refer Reply To:
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January 29, 2014

Legend

Parent =

Sub 1 =

Sub 2 =

Sub 3 =

Sub 4 =

Business A =

Business B =

Year 1 =

x =

y =

z =

Dear :

This letter responds to your representative's letter dated July 31, 2013, requesting rulings as to the Federal income tax consequences of a proposed transaction. Additional information was submitted by letters dated October 14, 2013 and November 5, 2013. The material information submitted for consideration is summarized below.

Summary of Facts

Parent, a publicly traded corporation, is the common parent of an affiliated group of corporations that has elected to file a consolidated federal income tax return (the "Parent Group") that includes both life insurance companies and nonlife insurance companies. The Parent Group is engaged in Business A. Parent owns all of the stock of Sub 1. Sub 1 owns all of the stock of Sub 3 and Sub 4. Sub 4 currently is disregarded as an entity separate and apart from its owner for federal income tax purposes under §301.7701-3 of the Procedure and Administrative Regulations. Sub 1 and Sub 3 are members of the Parent Group.

Sub 1 and Sub 3 each are primarily engaged in Business B. Sub 1 and Sub 3 are also engaged in the structured settlement business. In a structured settlement transaction, an assignee (i) assumes "qualified assignments" of personal injury liabilities within the meaning of section 130(c) of the Internal Revenue Code and (ii) purchases and holds annuity contracts that constitute "qualified funding assets" within the meaning of section 130(d).

Prior to the Year 1 Transaction (defined below), Sub 1 and Sub 2, a former direct subsidiary of Sub 1, assumed qualified assignments of personal injury liabilities within the meaning of section 130(c) and purchased annuity contracts, generally from each other, to hold as qualified funding assets within the meaning of section 130(d). In Year 1, in an effort to reduce costs and to simplify the Parent Group structure: (i) Sub 1 and Sub 2 transferred to Sub 3 the qualified assignment obligations, the ownership of the related annuities held as qualified funding assets, and cash in the approximate amount of a customary per-contract assignment company fee in exchange for constructive Sub 3 stock and the assumption of liabilities under such qualified assignments; and (ii) Sub 2 then merged into Sub 1, with Sub 1 surviving (the "Year 1 Transaction"). Prior to initiating the Year 1 Transaction, Parent received rulings with respect to the transaction.

As part of the Year 1 Transaction, claimants were asked to consent to a novation, i.e., to agree that Sub 3 could be substituted for Sub 1 or 2 (depending on which entity originally assumed the particular qualified assignment) as the primary obligor on the qualified assignment. Sub 1 guaranteed that payments would be made to claimants in accordance with the terms of their qualified assignments. Most claimants consented to a novation, but a minority objected to the novation (the “Year 1 Objectors”). Sub 1, on its own behalf and as successor to Sub 2’s obligations after the merger, remained liable to the Year 1 Objectors. Less than x% of the reserves for the qualified funding assets is attributable to the Year 1 Objectors.

Currently, Sub 3 is required to make periodic payments to claimants under the qualified assignment obligations assumed in the Year 1 Transaction. These payments are financed by the annuity contracts Sub 3 acquired in the Year 1 Transaction. In all cases, Sub 1, the issuer of the annuities held by Sub 3, directly pays the claimants, so that Sub 3 does not actually receive the annuity payments and issue its own payments. As part of a proposed entity consolidation plan, Sub 3 will merge with and into Sub 1. However, if Sub 3 were to merge into Sub 1 without any further adjustments of the structured settlements, the annuity contracts between Sub 1 and Sub 3 would be terminated by operation of law because the holder and issuer of the annuity contracts would become a single company. Accordingly, the taxpayer proposes the transaction described below (the “Proposed Transaction”). Taxpayer represents that the Proposed Transaction was not contemplated when the qualified assignments were made to Sub 1 and Sub 2 or at the time of the Year 1 Transaction. Taxpayer further represents that, prior to the Proposed Transaction, Sub 4 will elect to be treated as a corporation for federal tax purposes and thereafter will be a member of the Parent Group.

Proposed Transaction

The steps of the Proposed Transaction are as follows:

- (i) Sub 3 will send written notices to the claimants of the qualified assignment obligations (except the Year 1 Objectors). Each notice will indicate that the qualified assignment obligation owed to the claimant by Sub 3 will be transferred to Sub 4, unless the claimant objects within 30 days (the “Consent Period”); Sub 4 will replace Sub 3 as obligor on the qualified assignment obligation, i.e., the qualified assignment obligation will be novated; and as described in step (v) below, Sub 1 will guarantee that payments will be made to claimants in accordance with the terms of their qualified assignments.
- (ii) For all claimants, Sub 3 will transfer to Sub 4 (and Sub 4 will expressly assume) the qualified assignment obligations, the ownership of the related annuity contracts held as qualified funding assets, and cash in the approximate amount of a customary per-contract assignment fee in constructive exchange for Sub 4 stock and the assumption of liabilities under such qualified assignment obligations. Regulatory approval of the transfers will be obtained to the extent required.

(iii) For those claimants that do not object within the Consent Period, the transfers will result in a novation, i.e., Sub 4 will replace Sub 3 as obligor on each novated qualified assignment obligation. For those claimants that object within the 30-day period (and for the Year 1 Objectors), there will be no novation. When there is no novation, Sub 1, as Sub 3's successor following the merger described in step (v), will continue to be liable for the qualified assignment obligations. In all cases, consistent with current practice, payments to claimants will continue to be transmitted by Sub 1 (identified as the payor).

(iv) After the transfers of the qualified assignment obligations, annuity contracts, and cash described in Step 2, Sub 3 will merge into Sub 1 (the "Merger"), with Sub 1 surviving.

(v) Pursuant to board resolution, Sub 1 will guarantee that payments will be made to claimants in accordance with the terms of their qualified assignments as in effect immediately prior to the Year 1 Transaction.

Any objections of claimants to the assignment of the qualified assignment obligations are likely to precede the close of the Consent Period. However, it is possible that there might be errors in the notice procedure and that a small number of claimants might make valid objections after the close of the Consent Period. If such valid objections are made, any novations relating to such valid post-Consent Period objectors would be treated as void ab initio.

Representations

The following representations have been made in connection with the Proposed Transaction:

(a) The Merger will qualify as a statutory merger and therefore a reorganization under section 368(a)(1)(A).

(b) No stock or securities will be issued for services rendered to or for the benefit of Sub 4 in connection with the Proposed Transaction, and no stock or securities will be issued for indebtedness of Sub 4 that is not evidenced by a security or for interest on indebtedness of Sub 4 which accrued on or after the beginning of the holding period of Sub 3 for the debt.

(c) No stock will be transferred to Sub 4.

(d) Sub 3 has not accumulated receivables or made extraordinary payments of payables in anticipation of the Proposed Transaction.

(e) Sub 4 will report items, if any, that, but for the transfer, would have resulted in income or deduction to Sub 3 in a period subsequent to the transfer, and such items will constitute income or deductions to Sub 4 when received or paid by it. The proceeds received in collection of the income items will be included as ordinary income in computing the taxable income of Sub 4.

(f) The transfer of assets to Sub 4 is not the result of the solicitation by a promoter, broker, or investment house.

(g) Sub 3 will not retain any rights in the property transferred to Sub 4 in connection with the Proposed Transaction.

(h) The increase in the value of the Sub 4 stock as a result of any transfer of accounts receivable, if any, will be equal to the net value of the accounts transferred, i.e., the face amount of the accounts receivable previously included in income less the amount of the reserve for bad debts.

(i) The adjusted basis of the assets to be transferred by Sub 3 to Sub 4 will be equal to or exceed the sum of the liabilities to be assumed by Sub 4 (within the meaning of section 357(d)). For purposes of determining whether the adjusted basis of the transferred assets equals or exceeds the sum of the liabilities assumed by Sub 4, liabilities described in section 357(c)(3) are not taken into account.

(j) The fair market value of the assets to be transferred by Sub 3 to Sub 4 will exceed the sum of the liabilities to be assumed by Sub 4 (within the meaning of section 357(d)).

(k) The liabilities of Sub 3 to be assumed by Sub 4 (within the meaning of section 357(d)) were incurred in the ordinary course of business and are associated with the assets to be transferred.

(l) There is no indebtedness between Sub 4 and Sub 3, and there will be no indebtedness created in favor of Sub 3 as a result of the Proposed Transaction.

(m) The transfers and exchanges pursuant to the Proposed Transaction will occur under a plan agreed upon before the Proposed Transaction in which the rights of the parties are defined.

(n) All exchanges will occur on approximately the same date.

(o) There is no plan or intention on the part of Sub 4 to redeem or otherwise reacquire any stock constructively issued in the Proposed Transaction.

(p) Taking into account any issuance of additional shares of Sub 4 stock; any issuance of stock for services; the exercise of any Sub 4 stock rights, warrants, or subscriptions;

a public offering of Sub 4 stock; and the sale, exchange, transfer by gift, or other disposition of any of the stock of Sub 4 constructively to be received in the exchange, Sub 3 will be in “control” of Sub 4 within the meaning of section 368(c) immediately after the exchange.

(q) Although no Sub 4 stock will actually be issued, Sub 3 will receive constructive stock of Sub 4 approximately equal to the fair market value of the net assets transferred to Sub 4 (less any liabilities assumed by Sub 4 within the meaning of section 357(d)).

(r) Sub 4 will remain in existence and will retain and use the property transferred to it in a trade or business.

(s) There is no plan or intention by Sub 4 to dispose of the transferred property other than in the normal course of business operations.

(t) Each of the parties to the transaction will pay its own expenses, if any, incurred in connection with the Proposed Transaction.

(u) Sub 4 will not be an investment company within the meaning of section 351(e)(1) and § 1.351-1(c)(1)(ii) of the Income Tax Regulations.

(v) Sub 3 is not under the jurisdiction of a court in a title 11 or similar case (within the meaning of section 368(a)(3)(A)) and the stock or securities received in the exchange will not be used to satisfy the indebtedness of Sub 3.

(w) Sub 4 will not be a “personal service corporation” within the meaning of section 269A.

(x) The aggregate fair market value of the assets contributed by Sub 3 to Sub 4 will exceed such assets’ aggregate bases immediately after the Proposed Transaction.

(y) The fair market value of the assets of Sub 4 will exceed the amount of its liabilities immediately after the Proposed Transaction.

(z) The obligations originally assumed by Sub 1 and Sub 2 from defendants in lawsuits to pay liabilities to personal injury claimants were received by Sub 1 and Sub 2 in qualified assignments under section 130(c).

(aa) The annuity contracts issued by Sub 1 and held by Sub 3 to fund its obligations under qualified assignments met the requirements for qualified funding assets under section 130(d) when originally issued by Sub 1 to Sub 2 or by Sub 2 to Sub 1 and their terms have not been modified.

(bb) All terms and conditions of the obligations and qualified assignments originally entered into by Sub 1 and Sub 2 and all annuity contracts issued as qualified funding assets with respect to those obligations and qualified assignments issued by Sub 1 will be the same both before and after the Proposed Transaction.

(cc) No member of the Parent Group is subject to reporting obligations under section 6041 with respect to payments made to personal injury claimants on the qualified assignments because such claimants are eligible to exclude the damages under section 104(a)(2).

(dd) Sub 1 will guarantee that payments will be made to claimants in accordance with the terms of their qualified assignments as in effect before the Proposed Transaction.

(ee) The structured settlement business is less than y% of Sub 1's total business and less than z% of Sub 3's total business as measured by statutory reserves.

Rulings

Based solely on the information submitted and the representations set forth above, we rule as follows:

(1) No gain or loss will be recognized by Sub 3 on the transfer of assets to Sub 4 in constructive exchange for Sub 4 stock and the assumption (within the meaning of section 357(d)) by Sub 4 of liabilities associated with the structured settlements (sections 351(a) and 357(a)).

(2) No income, gain, or loss will be recognized by Sub 4 on the receipt of assets in exchange for the constructive receipt of its stock (section 1032(a)).

(3) The basis of each asset received by Sub 4 will be the same as the basis of that asset in the hands of Sub 3 immediately before the transfer (section 362(a)).

(4) The holding period of each asset received by Sub 4 will include the period in which the asset was held by Sub 3 (section 1223(2)).

(5) The basis of the Sub 4 stock constructively received by Sub 3 will be the same as the basis of the assets transferred by Sub 3 to Sub 4, decreased by the sum of the liabilities assumed by Sub 4 (as determined under section 357(d)) (sections 358(a) and (d)).

(6) The holding period of the Sub 4 stock constructively received by Sub 3 will include the period during which Sub 3 held the transferred assets, provided the transferred assets were held by Sub 3 as capital assets on the date of the transfer (section 1223(1)).

(7) Arrangements between Sub 1, Sub 3, and the claimants that previously qualified under section 130 will continue to qualify under section 130 after the pre-Merger transfers from Sub 3 to Sub 4.

(8) The Proposed Transaction will not subject Sub 4, Sub 1, or Sub 3 to information reporting under section 6041. This conclusion is based on the determination that the Proposed Transaction will not affect the continued applicability of the section 104(a)(2) exclusion from the claimants' gross income to the periodic payments, assuming that the exclusion applied before the Proposed Transaction.

(9) We decline to rule on the status of the annuities under section 72(q)(2)(G), 72(s)(5)(D), and 72(u)(3)(C). See Rev. Proc. 2013-1, Sec. 6.11, 2013-1 I.R.B. 1.

Caveats

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter.

Section 6.11 of Rev. Proc. 2013-1, states in part that generally a letter ruling will not be issued with respect to an issue that is clearly and adequately addressed by statute, regulations, decisions of a court, revenue rulings, revenue procedures, notices, or other authority published in the Internal Revenue Bulletin.

The rulings contained in this letter are based upon information and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. While this office has not verified any of the material submitted in support of the request for a ruling, it is subject to verification on examination.

Procedural Matters

This ruling is directed only to the taxpayers who requested it. Section 6110(k)(3) provides that it may not be used or cited as precedent.

A copy of this letter must be attached to any income tax return to which it is relevant. Alternatively, taxpayers filing their returns electronically may satisfy this requirement by attaching a statement to their return that provides the date and control number of this ruling letter.

In accordance with the power of attorney on file with this office, a copy of this letter is being sent to your authorized representatives.

Sincerely,

Mark J. Weiss

Mark J. Weiss
Reviewing Attorney, Branch 6
Office of Associate Chief Counsel (Corporate)